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No. 637

IN THE

Supreme Court of the United States

OCTOBER TERM, 1959

DOFSKIN PRODUCTS, INC. AND KUTA GAS & OIL COMPANY,
Petitioners

v.

WILLIAM D. PETTIT AND THOMAS J. CRAWFORD, TRUSTEES OF SWAN-FINCH OIL CORPORATION,
Respondents

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

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Petitioners, by their attorneys, pray that a writ of certiorari issue to review the judgments and orders of the United States Court of Appeals for the Second Circuit entered in this cause on August 24, 1959 and on October 13, 1959.

OPINIONS BELOW

The Findings of Fact, Conclusions of Law and Opinion of the District Court, dated November 10, 1958, (Applt's App., 113a) are not reported, and are set forth herein, together with the District Court's judgment, as Appendix A, *infra*, at p. 18. The opinions of the Court of Appeals, after argument and after petition for rehearing,

are reported at 270 F.2d 95 and 270 F.2d 699, respectively. (App. B and C, *infra*, at pp. 34, 48.)

JURISDICTION

The judgment of the Court of Appeals on appeal was entered on August 24, 1959 (App. B, *infra*, at p. 47). A petition for rehearing filed by petitioners was denied with opinion on October 13, 1959 (App. C, *infra*, at p. 48).

The jurisdiction of this Court is invoked under 28 USCA 1254(1) and 11 USCA 47.

QUESTIONS PRESENTED

1. Does an adverse claimant with a substantial interest in property in its possession but claimed by a trustee in a Chapter X proceeding waive its right to a plenary action theretofore asserted within *Cline* v. *Kaplan*, 323 U.S. 97, by the mere failure to cross-appeal from an order of the District Court denying on the merits the trustee's petition in a summary proceeding to have the adverse claimant turn over the property?

2. Is such an adverse claimant required to file a cross-appeal from a judgment of the District Court asserting jurisdiction over subject matter and dismissing the trustee's petition on the merits, in order to preserve on appeal its claim to a plenary action?

STATUTE INVOLVED

Section 2(a) of the Bankruptcy Act (52 Stat. 840), 11 USCA 11(a), confers upon all bankruptcy courts "such jurisdiction at law and in equity as will enable them to exercise original jurisdiction in proceedings under this Act . . . to . . . (7) cause the estates of bankrupts to be collected, reduced to money and distributed, and determine controversies in relation thereto . . ."

STATEMENT

William D. Pettit and Thomas J. Crawford are the qualified Trustees of Swan-Finch Oil Corporation, since January 2, 1958 a debtor in Chapter X proceedings under the Bankruptcy Act (11 USCA 501) pending in the United States District Court for the Southern District of New York.

Pettit and Crawford, respondents herein, will be referred to throughout this petition as the Trustees. They appealed to the Court of Appeals for the Second Circuit from an adverse judgment of the District Court, and secured a reversal which petitioners here seek to review. The debtor, also, filed an appeal with the Court of Appeals, and this petition is intended to apply to the debtor itself, wherever reference is made to the Trustees and the judgment of the Court of Appeals, insofar as the debtor may have standing independent of the Trustees.

Reference will be made in this petition to pages in the following printed appendices and briefs filed with the Court of Appeals, prior to its opinion and judgments: Appendix to Appellants' Briefs (Applt's App.); Appendix for Appellees (Appellees' App.); Brief of Appellants (Applt's Brief); Appellants' Reply Brief (Applt's Reply Brief); Appellees Brief (Appellees' Brief); Memorandum of Securities and Exchange Commission (SEC) and Petition for Rehearing (Rehearing).

Finally, it should be noted that the Securities and Exchange Commission participated in the proceedings in the District Court and the Court of Appeals.

On July 11, 1958 the Trustees secured an order from the District Court requiring Doeskin Products, Inc., hereinafter referred to as Doeskin or as petitioner, to show cause on August 8, 1958, or as soon thereafter as counsel could be heard, why an order should not be entered di-

recting it to turn over to the Trustees a certificate of stock (No. 3), allegedly delivered to it on September 16, 1955, for 1,143,090 shares (all of the issued and outstanding stock) of Keta Gas & Oil Company, also a petitioner here and hereinafter referred to as Keta. The order also required Doeskin and Keta to show cause why all of Keta's assets should not be turned over to the Trustees (Applt's App., 31a-35a).

Upon being served with the order to show cause, Doeskin and Keta, appearing specially, filed their cross-motion "to dismiss the proceeding on the ground that the Court lacks jurisdiction over the subject matter because there is a substantial adverse claim thereto which must be determined by plenary suit." (Applt's App., 36a). Doeskin and Keta, also, caused their attorneys to appear specially for the purpose of answering the Trustees' petition supporting the order to show cause, and in said answer Doeskin and Keta raised as a defense the Court's absence of summary jurisdiction over them or their property (Applt's App., 43a).

On September 9 and 10, 1958, the District Court held a summary hearing on the Trustees' claim to the Keta stock and assets. (Applt's App., 2a). This statement will refer at a later point to the evidence at the hearing. At the present, we limit ourselves to a description of petitioners' attempts to have their rights adjudicated in a plenary suit, instead of summarily.

At the close of the Trustees' proof, petitioners again moved to dismiss the proceeding, on the ground that the evidence demonstrated that Doeskin had a substantial interest in the Keta stock which could only be resolved in a plenary action. The District Court reserved decision on the motion (Applt's App., 102a-103a); and never entered an order with respect to it or the earlier written motion.

On November 10, 1958 the District Court filed its Findings of Fact, Conclusions of Law and Opinion (App. A, *infra*, p. 18) denying the Trustees' petition on its merits. In its Conclusions of Law, the District Court stated that it had jurisdiction of the parties and of the subject matter of the proceeding. On November 21, 1958 an order of the District Court was entered denying the Trustees' petition. (App. A, 31).

On the Trustees' appeal from this order, petitioners, in a separate point in their brief, specifically called the attention of the Court of Appeals to the fact that they have not waived "their right, if need be, to maintain their position disputing the jurisdiction exercised by the Court . . . However, as a caution, appellees respectfully submit that should reversal or substantial modification be indicated herein, a plenary action should be required instead of the instant proceeding." (Appellees' Brief, 33).

On August 24, 1959, the Court of Appeals filed its majority opinion, Judge Hand dissenting, reversing the District Court on the merits (App. B, *infra*, p. 34). No mention was made of appellees' right to a plenary action. Doeskin and Keta filed a timely petition for rehearing in which they again called the attention of the Court of Appeals to their right to a plenary action. On October 13, 1959 the Court of Appeals filed its opinion on the petition, denying it on the ground that District Court had implicitly denied petitioners' cross-motion to dismiss for lack of jurisdiction. The Court went on to write: "They [petitioners] may not so play fast and loose; if they meant to raise the point that the District Court was wrong to deny their cross-motion, they should have appealed from the order which denied it. *Peoria & P. U. Railway Co.* v. *United States*, 263 U.S. 528, 535, 536, 44 S. Ct. 194, 68 L.Ed 427."

We now concern ourselves with the factual details of the stock transaction involved. We refer throughout to

the factual findings of the District Court, which were adopted by the Court of Appeals with the observation that: "The basic facts are virtually undisputed." (App. B, *infra*, p. 35). We accept, for the purposes of this petition, this characterization of the evidence by the Court of Appeals, but append the *caveat* that the evidence was that produced by the Trustees in a summary proceeding in which petitioners had few of the safeguards provided for in a plenary action. So far as the Trustees' proof was concerned, petitioners had neither time nor opportunity to carry out discovery proceedings with respect to the facts. The Trustees and the Securities and Exchange Commission had the facts, so far as they were known; petitioners did not and had no way of getting them, except through their opponents' knowledge and records—an avenue which was, of course, closed to petitioners by the very nature of the summary proceeding. Accordingly, we set forth the facts upon which the District Court and Court of Appeals, one judge dissenting, reached opposing conclusions, and reserve for discussion the truly basic "fact" among them which proves to be not fact, at all, but fiction; *i.e.*, that the debtor received none of the proceeds of the stock manipulation.

In 1956-1957 one Lowell M. Birrell, now a fugitive from this country, controlled and dominated the affairs of Doeskin and the debtor corporation, Swan-Finch Oil Corporation, together with the debtor's subsidiaries. Doeskin and the debtor each had numerous public stockholders and the shares of each corporation was traded in the open market. Doeskin was and is engaged in the manufacture and sale of paper products. The debtor was a holding and operating company with a number of wholly-owned subsidiaries. One of its wholly-owned subsidiaries was, and is Swan-Finch Gas Development Corporation, hereinafter referred to as Gas Development. On September 27, 1955 the debtor was issued Stock Certificate No. 2 by Keta, for 1,140,390 shares of Keta stock, representing all of the issued and outstanding shares. (App. A, 20).

In December 1956, Birrell with assistance from dupes and scoundrels effected the transaction about which the Trustees complain. At the time Birrell was a director and the principal executive officer and agent of Doeskin. He was, also, a director and Treasurer of the debtor. Roy H. Callahan was President of Gas Development, and Mary B. Prior (Birrell's sister) was a director and Vice-President and Secretary of Gas Development. Callahan was, also, a director and the principal executive officer and agent of Keta. At all relevant times Birrell controlled and dominated the four corporations, through Callahan, Prior and other of his nominees to corporate positions. (App. A, 20).

On or about December 25, 1956 Birrell caused a contract to be executed in the names of Doeskin and Gas Development under date of October 5, 1956, in which Doeskin agreed to issue and sell 700,000 additional shares of its common stock to Gas Development, in consideration for all of the issued and outstanding shares of Keta, which Gas Development represented it owned. This agreement was signed by Birrell as Chairman of the Board of Directors of Doeskin, and by Callahan as President of Gas Development. (App. A, 20).

Doeskin corporate minutes showed that the Doeskin Board of Directors approved the agreement in a meeting held on December 31, 1956. The District Court decided that it was unable to find that such a meeting had, in fact, been held. Concerning the debtor, Callahan testified that he was present at a Board of Directors meeting on December 31, 1956 at which the agreement was approved. The District Court found that the agreement had been approved at a purported meeting of the debtor's directors on that date. (App. A, 22).

The District Court found that the agreement was effectuated in the following manner: On December 31, 1956 Birrell appeared with Callahan at the offices of Doeskin's

transfer agent and delivered a letter of instructions, signed by himself as Chairman of the Board of Doeskin, directing that seven certificates of 100,000 shares each of Doeskin common stock be issued in the name of Gas Development. This was done by the transfer agent and the seven certificates delivered to Callahan, who signed and delivered a receipt for them as president of Gas Development. Before they left the transfer agent's offices, Callahan turned the seven stock certificates over to Birrell. On the same day Callahan and Prior, acting as President and Secretary of Keta, issued its stock certificate No. 3 to Doeskin for all of Keta's issued and outstanding stock. (App. A, 22, 23).

The District Court found that at the time Callahan signed the agreement as president of Gas Development he was informed by Birrell, and believed, that the Keta stock had been conveyed previously by the debtor to Gas Development as a capital contribution. On or about September 27, 1955, the debtor had been issued Keta Stock Certificate No. 2 for all of Keta's issued and outstanding shares (1,140,390 shares). The District Court found that this certificate had been altered to show Gas Development as the holder, instead of the debtor, and Stock Certificate No. 3 then issued to Doeskin.

The certified public accountant of the debtor at the time testified that he had been shown minutes of meetings of the directors of the debtor and Gas Development, of January 4 and 26, 1956, respectively, purporting to show approval of the transfer by the debtor to Gas Development of the Keta stock; but the District Court found that such minutes had been manufactured by Birrell for the purpose of deceiving the accountant and that Keta, throughout 1956, did not cease to be a wholly-owned subsidiary of the debtor (App. A, 24).

Finally, the District Court found that between January 8, 1957 and March 28, 1957 all of the Doeskin stock re-

ceived by Gas Development had been transferred by Callahan or Prior, as President and Vice President of Gas Development, to Canadian transferees; and that "While there is no evidence with respect to the ultimate disposition of this stock, it can be reasonably inferred, and I find, that the stock of the proceeds thereof was used by Birrell in furtherance of his own purposes . . ." (App. A, 23).

This finding of fact, that Birrell used the Doeskin stock and its proceeds for his own use, became the keystone of the appellate court's conclusion that the debtor had never received possession of the stock or its proceeds, and was not, therefore, required to make restitution to Doeskin as a condition to recovery of the Keta stock. We submit that this crucial "fact", urged by the Trustees and S.E.C., is nothing more than a fiction which could muster as fact only in a drumhead 'summary' proceeding such as petitioners were unwillingly subjected to in the District Court.

Subsequent to the conclusion of the summary proceedings in the District Court the Birrell letter annexed to the Petition for Rehearing in the appellate court (at page 6) was brought to light. This letter makes it clear that Gas Development collateralized 50,000 of the Doeskin shares here involved for what must have been a substantial loan to itself on or about March 19, 1957. To this extent, at least, the debtor "possessed" the Doeskin shares and the conclusion of the appellate court is patently insupportable.

This Court's insistence that due process forbids the summary determination of substantial interests which are adverse to the Trustees bears wholesome fruit in a case like this. It inhibits the evil which must inevitably flow from the willingness of bankruptcy courts to treat the advocacy of a trustee as fact. Here, the District Court and the Court of Appeals, fully conscious of the failure

of the Trustees and the SEC to introduce proof of the ultimate disposition of the Doeskin stock, permitted themselves to accept the representations of partisans as fact. (Appellees' App., 23a, 24a, 29a; Applt's Brief, 7-8; Applt's Reply Brief, 8, 10; SEC, 4).

During the summary proceeding, petitioners, attempting to explore the facts within the restricted limits prescribed for them, cross-examined Callahan about an affidavit which he had previously executed in which he stated that approximately one-half of the Doeskin stock had been pledged by Gas Development to secure loans. He testified that he didn't know if this was actually true, but had relied on Birrell's assurance that it was true (Applt's App., 73a-75a). The District Court, relying upon the Trustees' representations, found that the affidavit was false, since "The appropriate 'evidence' and the 'hypothecation agreements' referred to in the above-quoted affidavit have never been adduced or substantiated" (App. A, 26).

The failure of proof was clearly that of the Trustees, and not of petitioners.

The District Court, in denying the Trustee's petition, concluded that, although Birrell manipulated the entire transaction, he had apparent authority to act for Doeskin and Callahan had apparent authority to act for Gas Development; that Doeskin parted with good and valuable consideration for the Keta stock; that it was not chargeable with Birrell's knowledge that Gas Development had defective title to the Keta stock, or that Birrell intended to divert the Doeskin stock to his own use; and that if Birrell's guilty knowledge was attributable to Doeskin, it was also attributable to the debtor and Gas Development, rendering it inequitable to permit the latter to rescind the transaction without restitution of the consideration paid by Doeskin.

The majority of the Court of Appeals differed from the District Court by concluding that the transfer of the Keta stock was entirely without authorization; and that the debtor was not required to tender back the Doeskin shares, because Callahan's "momentary token possession" was insufficient to constitute the debtor, or Gas Development, its wholly owned subsidiary, a possessor of the shares. Judge Hand, dissenting, was of the opinion that the delivery of the shares to Callahan as an officer of Gas Development, constituted the debtor a possessor of the shares, and required a restoration of the consideration received by the debtor.

REASONS FOR GRANTING THE WRIT

Although this Court has not directly ruled on the question, there seems to be no doubt that an adverse claimant in possession of property under a substantial claim of title is entitled, in a Chapter X proceeding as well as in an ordinary bankruptcy proceeding, to the safeguards of a plenary action in resisting the trustee's claim that the property belongs to the estate. Although the statute does not expressly refer to plenary actions, 11 USCA 11(a), this Court has long since held that the adverse claimant is entitled to such an action as a matter of due process. *Marshall* v. *Knox*, 16 Wall. 551, 556; *Tauble etc. Co.* v. *Fox*, 264 U.S. 426, 431; *Williams* v. *Austrian*, 331 U.S. 642, 647 fn. 9. Insofar as the courts of appeal have considered the question, they have asserted the adverse claimant's right to a plenary action. *In re Mantz TV*, (CA 7th 1955), 255 F.2d 489; *First National Bank of Houston* v. *Lake* (CA 4th 1952), 199 F.2d 524; *Duda* v. *Sterling Mfg. Co.* (CA 8th 1949), 178 F.2d 428.

Accordingly, the judgment below clearly transgresses the teaching of this Court in *Cline* v. *Kaplan*, 323 U.S. 97 with respect to an adverse claimant's right to a

plenary action, and the duty of a bankruptcy court to eschew summary jurisdiction once it is made aware of the claim's substance. The appellate court's views that petitioners were required to cross-appeal to preserve their jurisdictional defense, seems clearly to have been contrived for the purpose of avoiding the impact of the *Cline* case. It, also, violates long established authority, that an appellee need not, and cannot, take an appeal from a judgment which is favorable to it. *U. S. v. American Ry. Exp. Co.*, 265 U.S. 425, 435, 436.

In the *Cline* case at page 99, this Court reaffirmed previous decisions by writing: "Once it is established that the claim is not colorable nor frivolous, the claimant has the right to have the merits of his claim passed on in a plenary suit and not summarily."

Clearly, it must have been apparent at the outset to the District Court below that there was a substantial adverse interest opposed to the Trustees' claim. The Trustees' petition itself showed this, and petitioners' answer served to remove any lingering doubts. (Applts' App., 7a, 43a); and in retrospect, we find that two of the four judges who have ruled upon petitioners' interests have found them not only substantial, as opposed to colorable, but actually superior to those of the Trustees. Certainly, when these petitioners cross-moved to dismiss the Trustees' summary petition, there was ample ground for the District Court to grant their motion, so long as it heeded this Court's monition that an adverse claim may be said to be colorable only when "admitting the facts to be as alleged by the claimant, there is, as a matter of law, no adverseness in the claim. It is clear, however, that an actual claim may be adverse and substantial even though in fact 'fraudulent and voidable'. . . We are of the opinion that it is to be deemed of a substantial character when the claimant's contention 'discloses a contested matter of right, involving some fair

doubt and reasonable room for controversy', . . . in matters either of fact or law; and is not to be held merely colorable unless the preliminary inquiry shows that it is so unsubstantial and obviously insufficient, either in fact or law, as to be plainly without color of merit, and a mere pretense." *Harrison* v. *Chamberlin*, 271 U.S. 191, 194, 195.

It cannot be argued reasonably that petitioners left any stone unturned in seeking to impress either the District Court or the appellate court with their refusal to consent to the asserted summary jurisdiction. They appeared specially to cross-move for dismissal prior to the hearing, they appeared specially to answer that the District Court lacked summary jurisdiction, they moved orally to dismiss the rule at the close of the Trustees' proof, and they renewed their objections in their appellate brief. Appellate court below aborts this unequivocal position on the part of the petitioners, however, by laying sole emphasis on petitioners' failure to cross-appeal from the judgment of the District Court.

In this the appellate court's reliance on the *Peoria & P. U. Ry. Co.* v. *United States*, 263 U.S. 528, is wholly misplaced. Justice Brandeis carefully noted in *U.S.* v. *American Ry. Exp. Co.*, *supra*, footnote at p. 436, that the decision in the *Peoria* case, written by him only months previously, "rests upon the peculiar character of the question raised." The *Peoria* case dealt with the narrowest of venue points, raised no question of importance to the subject matter, and, it may be fairly stated, presented implications that the United States and its *alter ego*, the Interstate Commerce Commission, were straddling the issue of venue for tactical advantage.

The *American Railway* case is pertinent where the *Peoria* case is not: for it makes clear that an appellee has no duty to cross-appeal from a judgment which does not aggrieve it, in order to sustain the result of the

judgment (the dismissal of the Trustees' petition) upon other grounds than that adopted by the trial court. In *American Railway*, that express company obtained a temporary injunction in the District Court against an order of the Interstate Commerce Commission, on the ground that the order was erroneously based upon a finding that the express company was not a "carrier" within the meaning of the pertinent statute. On appeal, the company claimed that the order was void on other grounds, also. Appellants argued that these grounds could not be considered, because they had been overruled by the District Court and appellee had not taken a cross-appeal. This Court ruled that the appellee may, "without taking a cross-appeal, urge in support of a decree any matter appearing in the record, although his argument may involve an attack upon the reasoning of the lower court or an insistence upon matter overlooked or ignored by it." 265 U.S. 425, 435. *Langnes* v. *Green*, 282 U.S. 531, 538.

Petitioners here had no adverse decree upon which to cross-appeal. Far from being aggrieved, the District Court had favored them beyond their pleas by dismissing the Trustees' petition on the merits. All that they were required to do, in fairness to the appellate court and in preservation of their rights to a plenary action, they did by raising the point clearly in their brief. We submit that the right to support the judgment below, in the absence of a cross-appeal, extends to the part, as well as to the whole; and thus entitled petitioners to have the appellate court affirm the dismissal on the constitutional ground raised below and preserved in the brief.

Not only was there no duty upon petitioners to cross-appeal from the District Court's judgment, but it is clear that they had no legal right to do so. Indeed, the same appellate court has previously dismissed a cross-appeal by an objecting creditor to an order of the District Court denying a discharge to a bankrupt, on the ground that

the objecting creditor had achieved his full measure of relief in the denial of the discharge, despite the overruling of one of the grounds advanced by the objecting creditor. *In re Schwartz* (CCA 2d 1937), 89 F.2d 172. The court there wrote, at page 173, "A successful litigant is not injured, and may not appeal, merely because a court has rejected or failed to adopt some of his contentions," and observed that the rule of the *American Railway* case protected the appellee's right to support the result below by anything in the record. *Aberly* v. *Craven County* (CCA 4th 1934), 70 F.2d 52; *Williams* v. *Bank of America Nat. Ass'n* (CCA 2d 1932), 55 F.2d 884.

There remains for discussion the view of the appellate court below that the judgment of the District Court was intended to embody a denial of petitioners' cross-motion, and there was, therefore, in existence an adverse order upon which petitioners could, and should, have filed a cross-appeal. We respectfully submit that the judgment clearly did not embody such an adverse order, and the conjuring up of such an alleged order serves no necessary or desirable purpose in appellate jurisprudence. Indeed, it creates a mischievous precedent which can only produce unnecessary and burdensome cross-appeals by anxious and confused counsel. In the instant case it unfairly strikes a death blow at petitioners' harried attempts to enjoy their unquestionable right to a plenary action with the safeguards of procedural due process. We do not understand how the appellate court may reason that the District Court's finding of jurisdiction over the subject matter necessarily implies that it denied petitioners' cross-motion, which was based upon the ground of due process. The District Court had jurisdiction of the subject matter; but, in addition, it was required to exercise that jurisdiction in a plenary action.

The procedure adopted by the District Court, although fully and often apprized of petitioners' objection to its

summary proceeding, was certainly not an orderly one, insofar as that issue was involved. The trial judge made no attempt to hold a preliminary hearing on the issue, which is usually done and which he did in a companion case to this one. See the decision of the appellate court below in *Petfit* v. *Oleon Industries, Inc.* 266 F. 2d 833. See, also, that this was the procedure followed in *Cline* v. *Kaplan, supra,* affirming 142 F.2d 301, *sub. nom. In re Gold Medal Laundries* (CCA 7th 1944).

If, indeed, the District Court intended to enter a final order denying the plenary claim and putting petitioners on notice that a cross-appeal was required, more was required than the record now shows. It was the Trustees' obligation to see that such an order was entered, for it favored them. In addition, there is no answering objection by the Trustees' in their briefs to the petitioners' briefed contention that their rights to a plenary action persisted.

We see the appellate court's fiction of an adverse order only as a device to default petitioners despite the rule in the *American Railway* and related cases, and we submit that it produces only a grotesque and unworthy result. In contrast, we refer this Court to the solicitude exhibited by the First and Eighth Circuits to see that limitations placed upon an appellee by the existence of a favorable judgment below be not utilized "to accomplish an obvious injustice." *Cochran* v. *M. & M. Transp. Co.* (CCA 1st 1940), 110 F.2d 519, 521; *Guarantee Co. of North America* v. *Phenix Ins. Co.* (CCA 8th 1903), 124 Fed. 170; *cf. Rogers* v. *Penobscot Mining Co.* (CCA 8th 1907), 154 F. 606.

Concluding, we submit that these petitioners have received no more than lip service, with respect to their rights to a plenary action. Restricted to such facts as the Trustees saw fit to divulge, they have been stripped of their property without their day in court; and the

deprivation has been affirmed upon rehearing, even in the knowledge that the basic "fact" rammed home by overzealous Trustees is not fact at all. Firally, the appellate court below has seen fit unreasonably to charge petitioners with playing "fast and loose", because of their insistence upon their rights.

It has been 15 years since this Court found it necessary to review the *Cline* case, because of its importance to bankruptcy administration. The proceedings and judgment below make it plain that there is again need for this Court's review of the procedures which are reasonably required to protect adequately an adverse claimant in his rights to due process in Chapter X proceedings.

CONCLUSION

For the above reasons, it is respectfully submitted that this petition for a writ of certiorari should be granted.

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APPENDIX A

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

In the Matter
of
SWAN-FINCH OIL CORPORATION,
Debtor

In proceedings for Reorganization of a Corporation

No. 93046

FINDINGS OF FACT

1. The petitioners are trustees of the Swan-Finch Oil Corporation, a debtor in reorganization proceedings pursuant to Chapter X of the Bankruptcy Act. They have duly qualified and are now acting as such pursuant to order of this Court.

2. The debtor herein, Swan-Finch Oil Corporation (Swan-Finch), is a corporation organized and existing pursuant to the laws of the State of New York, with its principal place of business at 41 East 42nd Street, New York, New York. At all times relevant hereto, it was a holding and operating company with a number of wholly-owned subsidiaries.

3. Keta Gas and Oil Company (Keta) is a corporation organized and existing pursuant to the laws of the Commonwealth of Pennsylvania. During all of the times herein referred to, it was engaged in the business of owning acreage and developing and drilling gas wells. At various periods of time it maintained offices and trans-

acted business at Bradford, Pennsylvania, and at 41 East 42nd Street, New York, New York. All its financial affairs were conducted from its executive offices at 41 East 42nd Street, New York, New York, and at various times it maintained active bank accounts in New York, New York. It is present within the jurisdiction of this Court. *French* v. *Gibbs Corp.*, 189 F. 2d 787 (2d Cir. 1951).

4. Swan-Finch Gas Development Corporation (Gas Development) is a corporation organized and existing pursuant to the laws of the Commonwealth of Pennsylvania, with an office for the transaction of business at 545 Fifth Avenue, New York, New York. At all times relevant hereto, it was a wholly-owned subsidiary of the debtor, Swan-Finch.

5. Doeskin Products, Inc. (Doeskin) is a corporation organized and existing pursuant to the laws of the State of New York and at all times relevant hereto has been engaged in the manufacture and sale of paper products, with an office for the transaction of business at 41 East 42nd Street, New York, New York.

6. During the period of the transactions referred to herein, Swan-Finch and Doeskin were public corporations with numerous stockholders, the stock of which corporations was purchased, sold, and traded on the open market.

7. For some time prior to September 27, 1955, and during the period relevant hereto, one Lowell M. Birrell (Birrell) was a director, and the principal executive officer and agent of Doeskin; and as such he dominated and controlled said corporation through his nominees and designees. For some time prior to September 27, 1955, and until October 1, 1956, Birrell was a director and the principal executive officer and agent of Swan-Finch; and as such he dominated and controlled said corporation through his nominees and designees. From October 1,

1956, and during the period relevant hereto, Birrell was a director and Treasurer of said corporation. During this period he continued to dominate and control said corporation through his nominees and designees. During the period referred to in Findings 10 and 11 hereof Birrell was a director of Gas Development. He dominated and controlled said corporation through his nominees and designees, among them, Roy H. Callahan (Callahan) who was President of said corporation and Mary B. Prior (Prior), who is Birrell's sister and who was a director and Vice President and Secretary of said corporation.

8. On or about September 27, 1955, Swan-Finch became the owner of all the issued and outstanding stock of Keta, represented by Certificate #2 for 1,140,390 shares.

9. Thereafter, Birrell became and, until some time prior to October 1, 1956, continued to be a director, and the principal executive officer and agent of Keta; and as such he dominated and controlled said corporation through his nominees and designees. At some time prior to October 1, 1956, and during the period relevant hereto, Callahan became and continued to be a director and the principal executive officer and agent of said corporation; but Birrell continued to dominate and control said corporation through his nominees and designees, among them Callahan.

10. From on or about December 25, 1956 until on or about March 28, 1957 Birrell, by virtue of his said dominance and control of the above corporations, was able to effect the following transactions for his own purposes and without regard to the interests of the corporations involved or of their respective stockholders:

(a) On or about December 25, 1956 he caused an agreement to be signed for the sale of all the issued and outstanding stock of Keta by Gas Development to Docskin.

This agreement was signed by Birrell as Chairman of the Board of Directors of Doeskin and by Callahan as President of Gas Development. The agreement provided for the sale to Doeskin by Gas Development of all the issued and outstanding stock of Keta in return for 700,000 shares of Doeskin. Provision was included for an adjustment of the number of shares of Doeskin to be transferred to Gas Development. This agreement was pre-dated October 5, 1956 and its contents were revealed for the first time by Birrell to Callahan subsequent to December 15, 1956. At the time said agreement was executed Birrell represented to Callahan, and Callahan believed, that the stock of Keta had been conveyed to Gas Development by Swan-Finch as a capital contribution.[1] Certificate No. 2 of Keta, purporting to evidence the ownership by Gas Development of Keta, is signed by Birrell as President of Keta and by Prior as Secretary of Keta. It is the certificate referred to in Finding 8, above, and is dated September 27, 1955. The name of the holder has been changed in typescript on its face from "Swan-Finch Oil Corporation" to "Swan-Finch Gas Development Corporation" by striking out of the word "Oil" and the interlineation of the words "Gas Development." The stub of the certificate shows on its face a similar change, apparently in the handwriting of Prior, and effected by striking the word "Oil" and inserting the words "Gas Devt."

(b) On December 28, 1956 Birrell recommended to the Board of Directors of Doeskin that the agreement dated October 5, 1956, be approved. As the result of the resignation of a number of Doeskin directors at this meeting, the meeting was postponed until December 31, 1956, at which time the postponed meeting, according to minutes now in existence, took place. These minutes are signed by one John W. Crosby (Crosby) as Secretary of Doeskin and purport to show that Birrell, Callahan, and Crosby

[1] See Finding 11 within.

were the directors in attendance, and that they approved the agreement. Callahan denied, under oath, at the hearing before this Court, that he attended such a meeting. Birrell has evaded the process of this Court and consequently was not produced as a witness. Crosby was not produced as a witness for reasons which do not appear in the record. Accordingly, I am unable to find that the postponed meeting was held.

(c) The agreement for the sale of Keta to Doeskin was approved at a purported meeting of the Board of Directors of Swan-Finch on December 31, 1956, attended by Birrell, Prior, and Callahan. Another director, one William M. Erb (Erb), was present according to the testimony of Callahan. Erb appeared as a witness at the hearing before this Court and denied his presence at the meeting. The minute book of Swan-Finch contains no minutes of such a meeting. Ralph E. Damp (Damp), who was President and a director of Swan-Finch at the time of this meeting, had no knowledge of it nor did he receive any notice thereof. Edward G. Brown (Brown), Executive Vice President and a director of Swan-Finch at the time of this meeting, had no knowledge of it nor did he receive any notice thereof.

(d) Manufacturers Trust Co. was transfer agent for the common stock of Doeskin in December 1956 and for some time subsequent thereto. On December 31, 1956, Callahan and Birrell called at the corporate trust department of Manufacturers Trust Co. and obtained possession of 700,000 shares of $1.00 par value Common Stock of Doeskin registered in the name of Gas Development against a receipt signed by Callahan as President of Gas Development. Among the documents tendered to Manufacturers Trust Co. at this time were (1) a letter of instructions signed by Birrell as Chairman of the Board of Doeskin, authorizing and directing Manufacturers Trust Co. to prepare the seven certificates of 100,000

shares each of Doeskin Common Stock in the name of Gas Development; and further authorizing delivery thereof to a representative of Gas Development; and (2) a letter addressed to Doeskin on the stationery of Birrell and Larson, as attorneys, counsel for Doeskin, signed, apparently in the handwriting of Birrell, "Birrell & Larson," and certifying to the regularity of various corporate procedures relating to Doeskin and Gas Development with a view to the consummation of the agreement above referred to. Upon the request of Birrell, and in the office premises of the Manufacturers Trust Co., on December 31, 1956, Callahan turned over the certificates of Doeskin stock to Birrell.

(e) On December 31, 1956, Certificate No. 3 of Keta was issued in the name of Doeskin. This certificate, representing all the issued and outstanding stock of Keta, was signed by Callahan as President, and Prior as Secretary, of Keta.

(f) Between January 8, 1957 and March 28, 1957, all of the aforesaid Doeskin stock was assigned to transferees in Montreal and Toronto, Canada. The certificates of transfer bear the signatures of Prior as Vice President and Callahan as President of Gas Development. While there is no evidence with respect to the ultimate disposition of this stock, it can reasonably be inferred, and I find, that the stock or the proceeds thereof was used by Birrell in furtherance of his own purposes and in derogation of the rights of the corporations involved and their stockholders.

(g) Throughout all of the transactions herein described, Birrell was the sole actor, whereas Callahan and Prior were dominated by him and consistently performed whatever acts were sought by him.

11. Harvey M. Coltin, Certified Public Accountant for Swan-Finch, some time between January and April 1957,

sought confirmation of the transaction resulting in the transfer of Keta stock from Swan-Finch to Gas Development and was unsuccessful in his attempts to communicate with Birrell for this purpose or for any other. He requested confirmation of the transaction from Prior, and some weeks after he first raised the question with Prior, he was shown minutes of Swan-Finch dated January 4, 1956 and purporting to authorize the transfer of the Keta stock to Gas Development. These minutes cannot now be found. He was also shown (1) minutes of Gas Development dated January 26, 1956, and signed by Prior as Secretary, purporting to report a meeting of Gas Development at which Brown presided and at which the Keta stock was accepted by Gas Development; and (2) a letter of the same date from Swan-Finch, signed by Birrell, stating that the Keta stock was being transferred. This letter was signed by Prior on behalf of Gas Development. It is reasonable to infer, and I find, that these documents were manufactured for the purpose of deceiving Coltin. This finding is supported by (1) the manner in which the Keta certificate was altered (see Finding 10(a) above); (2) the fact that those copies of the minutes of the Swan-Finch meeting at which the transfer to Gas Development was allegedly approved (January 4, 1956) which are now in existence, which copies were sent to Brown and to Swan-Finch's attorney, Grant, immediately after the meeting, contain no such resolution; (3) the fact that Brown and Grant denied, at the hearing before the Court, that the transfer of Keta stock to Gas Development was discussed or approved at the January 4, 1956 meeting of Swan-Finch, at which both were present;[2] (4) the fact that Brown denied, at the hearing before the Court, that he had presided or been present at the

[2] The minutes show that Birrell and Prior were the only others present at this meeting. Both of these persons have been evading the process of this Court and neither was called as a witness at the hearing.

purported January 26, 1956 meeting of Gas Development;[3] (5) the fact that Swan-Finch, in statements to the public and to its shareholders after January 4, 1956, continued to refer to Keta as a wholly-owned subsidiary of Swan-Finch; (6) the fact that to the knowledge of Damp, President of Swan-Finch from October 1, 1956, Keta did not cease to be a wholly-owned subsidiary of Swan-Finch during 1956; and (7) the lack of independent evidence of the existence of these documents before January, 1957.

12. On July 22, 1957, Callahan swore to an affidavit in connection with a Swan-Finch stockholders' derivative action then pending in the Supreme Court of the State of New York. That affidavit states in part as follows:

> "Subsequently, Swan Finch Gas Development Corporation, a subsidiary of Swan Finch Oil Corporation and a company which had acquired all of the stock of the Keta Gas and Oil Company, transferred its Keta Gas and Oil Company holdings to Doeskin Products, Inc. in exchange for 800,000[4] shares of Doeskin Products, Inc. stock. This transaction is being attacked by Swan Finch Oil Corporation stockholders on the ground that the contract was inadequate. It is being attacked by Doeskin Products,

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[3] The minutes show that Birrell, Prior, and one John W. Meyer were also present. Birrell and Prior are evading the process of this Court and neither was produced at the hearing. Meyer was not produced for reasons which do not appear in the record.

[4] On February 4, 1957, Doeskin, in a letter signed by Birrell as Chairman of the Board, advised Gas Development that "you owe us no additional cash and we owe you no additional stock." This letter was accepted by Callahan as President of Gas Development. The agreement dated October 5, 1956 provided for the transfer of 700,000 shares of Doeskin. See Finding 10(a). There is no evidence, aside from the quoted portion of Callahan's affidavit, and a statement in Doeskin's Annual Report for 1957, that more than 700,000 shares of Doeskin were transferred; and despite the reference in the letter of February 4, 1957 to "additional cash", there is no evidence that any cash changed hands in this transaction nor does the agreement dated October 5, 1956 provide for the transfer of any cash.

Inc. stockholders on the ground that the contract was excessive. Both allegations cannot be true. I state that the transaction, in my opinion, was fair and reasonable and was in the best interest of Swan Finch Oil Corporation and at the proper time, as an officer and director of the Company which participated in the disposition by Swan Finch Gas Development Company of its Keta Gas and Oil Company holdings to Doeskin Products, Inc., I will be prepared to justify the transaction by appropriate evidence. * * *

"Such stock was issued to and owned by Swan Finch Gas Development Corporation. After such acquisition all of such stock was hypothecated. As of the present time approximately one-half of such stock has been disposed of by pledges and accountings for the proceeds thereof have been made or are now in process of being made. The remainder of such stock is still held by pledgees under hypothecation agreements."

These statements were composed by Birrell and were sworn to by Callahan on Birrell's representation that they were true. It is reasonable to infer from the record of the hearings held before this Court, and I find, that the purport of these statements was false and untrue and was known to be such by Birrell at the time. The "appropriate evidence" and the "hypothecation agreements" referred to in the above-quoted affidavit have never been adduced or substantiated.

Conclusions of Law

1. This Court has jurisdiction of the parties and of the subject matter of this proceeding.

2. Callahan had apparent authority from Gas Development to sell the stock of Keta. Birrell had apparent authority from Doeskin to purchase the stock of Keta and to pay for the Keta stock with Doeskin stock. Callahan had apparent authority to receive the Doeskin stock on behalf of Gas Development.

3. Doeskin parted with good and valuable consideration in return for its acquisition of the Keta stock.

4. Doeskin may not be charged with the knowledge of its agent, Birrell, that Gas Development had defective title to the Keta stock, or with his knowledge that the consideration for the sale of the Keta stock was never intended to remain with Gas Development but was intended to be diverted to his own use after its receipt by Gas Development, the wholly-owned subsidiary of the debtor.

5. Assuming Doeskin could be charged with Birrell's guilty knowledge, Swan-Finch and Gas Development are also chargeable with the same knowledge, thereby rendering it inequitable to permit Swan-Finch or Gas Development to rescind the Keta sale without restitution of the consideration paid by Doeskin.

6. Respondents are entitled to judgment and an order denying the motion.

Discussion

This proceeding has been brought on by an order to show cause issued July 11, 1958 directing Doeskin and Keta to show cause why Doeskin should not be directed to turn over to the trustees of Swan-Finch the certificate representing all the outstanding stock of Keta; and the assets of Keta. On the basis of the facts, as I have found them, I am unable to conclude that the trustees are entitled to this relief.

It is clear that Doeskin parted with substantial consideration in acquiring the Keta stock. While there is no evidence in the record to indicate the relative values of the Keta and Doeskin stock on December 31, 1956, it is reasonable to infer that they were substantial and that the Doeskin stock, which was ultimately transferred to Canada, was worth substantially more than $6,000,000.00

in the period January-March 1957. The trustees are not in possession of this stock and are incapable of restoring it to Doeskin as a condition for the return of the Keta stock. Indeed, the position of the trustees is that they should be declared the rightful owners (on behalf of Swan-Finch) of the Keta stock and that restitution of the Doeskin stock cannot be required as a condition precedent to the return of the Keta stock. Moreover, restoration of the parties to the *status quo ante*, even if it were possible, might be inequitable on the ground of changed circumstances subsequent to the transactions detailed in the Findings of Fact, for it has been alleged that Keta, since its acquisition by Doeskin, has been looted and despoiled by Birrell. See A.L.I., Restatement of the Law of Restitution § 142 (1937).

I believe that the entire transaction, from its initial stages, was executed by Birrell with larcenous intent. The trustees, while not disputing this, maintain (1) that Doeskin never got title to the Keta stock because Gas Development never had title to pass and that this lack of title was evident from the altered face of the certificate; and (2) that Doeskin cannot be considered a bona fide purchaser for value because it must be charged with

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[5] Although there has been an absence of proof on this point, the only Doeskin officer or agent who may be said to have had knowledge of the alteration on the face of the certificate was Birrell.

Reliance by the trustees on N. Y. Pers. Prop. Law § 177, is misplaced. We are dealing here with an agent of the owner, possessing apparent authority and acting pursuant to apparently valid contractual arrangements. Section 177, however, enacts the common law rule, equally inapplicable here, concerning the effect of the alteration of a stock certificate by a thief is a stranger to the true owner. *National Surety Co.* v. *Indemnity Ins. Co. of North America*, 237 App. Div. 485, 261 N. Y. Supp. 605 (1st Dept. 1933). *Cf. Glenn L. Martin Co.* v. *Fidelity-Baltimore National Bank and Trust Co.*, 27 U. S. L. Week 2212 (Md. 10/24/58). Moreover, the statute makes specific reference to the law of principal and agent, which is applicable here. N. Y. Pers. Prop. Law § 179.

the knowledge of its Chairman of the Board (Birrell) (a) of the defect in title, and (b) that the consideration for the Keta stock was never intended to remain in the hands of Swan-Finch or Gas Development but was destined for the pocket of Birrell. I am unable to conclude, however, as the trustees urge, that Doeskin must be considered *particeps criminis* with Birrell or that Swan-Finch may disaffirm Birrell's actions while Doeskin must be saddled with their consequences.

Swan-Finch may disaffirm Birrell's actions in transferring the Keta stock to Gas Development and in converting the Doeskin stock to his own use, because in performing these acts Birrell was furthering his own purposes and was not acting within the scope of his agency for Swan-Finch. By a parity of reasoning, however, Doeskin cannot be held to Birrell's knowledge of the steps he had taken or was to take to further this scheme. The theory is that an agent does not inform his principal of acts which it is in the agent's interest to conceal. *Carlisle* v. *Norris*, 215 N. Y. 400, 109 N. E. 564 (1915); *Brooklyn Distilling Co.* v. *Standard Distilling and Distributing Co.*, 193 N. Y. 551, 86 N. E. 564 (1908); A. L. I., Restatement of the Law of Agency § 282 (1933).

On the other hand, it may be said that in order to justify retention of the Keta stock by Doeskin, it must be charged with Birrell's knowledge, since Doeskin's title to the Keta stock stems from the purchase in which Birrell acted as Doeskin's agent. The theory is that Doeskin cannot at once affirm Birrell's acts in consummating the purchase, and disaffirm his knowledge that Gas Development did not have title and that the consideration for the purchase was not to remain with Swan-Finch or Gas Development. *Maurer* v. *Harriman*, 85 F. 2d 493, 495 (2d Cir.), *cert. denied*, 299 U. S. 601 (1936). See also, *Wilcox* v. *Gaess*, 92 F. 2d 8, 10-11 (2d Cir. 1937), *cert. denied*, 303 U. S. 647 (1938). This reasoning is applicable, how-

ever, *pari passu*, to the trustees' position in relation to Doeskin's demand for the return of its stock as a condition to the surrender of the Keta stock to the trustees. The trustees can resist this demand only by setting up the title to the Doeskin stock which was received by Gas Development and thus impliedly affirming Birrell's acts. Swan-Finch, then, must also be held to Birrell's knowledge of the defect in Gas Development's title and to his plan for the subsequent disposition of the Doeskin stock and must be held to have ratified Birrell's acts.[6]

Decision, in a case of this sort, on the basis of the principals' knowledge, or lack thereof, of their agent's acts, is, of course, fictional. *Munroe* v. *Harriman*, *supra* at 495. The fiction is, however, useful in determining who must bear the burden of Birrell's depredations. This is not a case, as was *Harriman*, in which an innocent party was defrauded by another party's agent. Birrell was the dominating and controlling force in each corporation and each or none must bear the consequences of his acts. Birrell, thoughout the entire transaction, was the sole actor, Callahan and Prior having been dominated by him and having consistently performed whatever acts were sought by Birrell. No applicable principle of law or equity places either of these corporations in a superior position in relation to the other or justifies a ruling that either set of shareholders must bear the burdens of Birrell's wrongdoings. The trustees' clean hands do not shield Swan-Finch from the consequences of Birrell's acts. Equity decrees that although "the hand receiving [the proceeds] be ever so chaste, yet, if it comes through a polluted channel, the obligation of restitution will follow

[6] The trustees' contention that they may resist a demand for the return of the Doeskin stock on the theory that they never received it, is not consonant with the facts. See Finding of Fact 10(d) above. Throughout the entire transaction Gas Development was the wholly-owned subsidiary of Swan-Finch and both were dominated and controlled by Birrell.

it."[7] While this maxim may no longer hold in many situations, it is applicable here. Since restitution is impossible, I am forced to leave the parties as I find them, with their remedies against the wrongdoer—remedies, I am all too aware, which appear now to be illusory.

An appropriate order will be entered. Since the trustees of Swan-Finch might suffer irreparable damage if the Keta certificate, now in the custody of this Court, were to be removed therefrom, and this decision later modified or reversed, the order will contain an appropriate stay pending the disposition of the appeal which I have been advised the trustees wish to take.

Settle order on notice.

Dated: New York, N. Y.
November 10, 1958.

EDMUND L. PALMIERI,
U. S. D. J.

ORDER

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

[SAME TITLE]

At New York, New York, in said District
on the 20th day of November, 1958.

WILLIAM D. PETTIT, one of the Trustees of the debtor herein, having presented and filed a petition dated and

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[7] The quotation is from Lord Chief Justice Wilmot's opinion in *Bridgman v. Green*, and is found in *Huguenin v. Baseley*, 14 Ves. 273, 289, 33 All E. R. 526, 432 (Chancery, 1807).

verified the 10th day of July, 1958, for an order directing the respondent, Doeskin Products Inc., to turn over to the petitioner a certain certificate of stock of Keta Gas & Oil Company, bearing Number 3 for 1,143,390 shares and directing Doeskin Products, Inc. and Keta Gas & Oil Company, the respondents herein to turn over to the petitioner leases and interests in gas wells, fixtures, equipment, supplies, acreage and installations pertinent to the development and maintenance of gas wells, together with cash and accounts receivable, and an order having been made thereon dated July 11, 1958, by Hon. Edmund L. Palmieri, United States District Judge, directing Doeskin Products, Inc., and Keta Gas & Oil Company, as respondents, to show cause why such relief should not be granted, and the said Doeskin Products, Inc. and Keta Gas & Oil Company having filed their answer verified the 7th day of August, 1958, with respect to the said petition, and the proceeding having come on to be heard before the said District Judge, and George C. Levin, Esq., attorney for the Trustees having appeared for the petitioners, and Kaye, Scholer, Fierman, Hays & Handler, Esqs., attorneys for the debtor having appeared by Milton Kunen, Esq., and Joseph Moscou, Esq., and the Securities Exchange Commission having appeared by Kiva Berke, Esq., its attorney, and McCarthy, Kapelman & Nathanson, Esqs., attorneys for the respondents having appeared by Isadore Nathanson, Esq. and Milton Paulson, Esq., and hearings having been held before the said District Judge on September 9 and September 10, 1958, and oral arguments having been held before the said District Judge on the 22nd day of October, 1958, and the Court having duly rendered a decision in writing stating separately the facts found and the conclusions of law dated the 16th day of November, 1958.

Now, on motion of McCarthy, Kapelman & Nathanson, attorneys for the respondents, it is

ORDERED, ADJUDGED AND DECREED that the aforesaid petition of the Trustees dated July 10, 1958 be and the same hereby is in all respects denied, and it is further

ORDERED that the restraining order heretofore entered by this Court on June 20, 1958, and continued in effect by the aforementioned order of July 11, 1958, be and the same is hereby vacated, and it is further

ORDERED that this order of the Court be, and it hereby is stayed pending final determination of an appeal from this judgment on condition that said appeal be prosecuted diligently, and without prejudice to the rights of the respondents if said condition is not complied with, to move this Court for a vacation of this stay.

EDMUND L. PALMIERI,
U. S. D. J.

Judgment Entered November 21, 1958
HERBERT A. CHARLSON
Clerk

APPENDIX B

UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

No. 244—October Term, 1958.

(Argued February 11, 1959 Decided August 24, 1959.)

Docket No. 25437

WILLIAM D. PETTIT and THOMAS J. CRAWFORD,
Trustees-Appellants,

—v.—

DOESKIN PRODUCTS, INC. and KETA GAS & OIL COMPANY,
Appellees.

B e f o r e :

HAND, *Circuit Judge*,
MADDEN, *Judge*, United States Court of Claims,*
and LUMBARD, *Circuit Judge*.

The trustees of Swan-Finch Oil Corporation appeal from a denial by the District Court for the Southern District of New York, Edmund L. Palmieri, *J.*, of their motion to compel Doeskin Products, Inc. and Keta Gas & Oil Company to turn over to them all the stock and assets of Keta.

Reversed and remanded.

* Sitting by designation pursuant to the provisions of 28 U. S. C. § 291(a).

GEORGE C. LEVIN and MILTON KUNEN, New York, N. Y. (James T. Sherwin, Joseph J. Moscou and Kaye, Scholer, Fierman, Hayes & Handler, New York, N. Y., on the brief), *for trustees-appellants.*

I. Z. NATHANSON, New York, N. Y. (Samuel Aleyner, Gerald Kahn and McCarthy, Kapelman & Nathanson, New York, N. Y., on the brief), *for appellees.*

LUMBARD, *Circuit Judge:*

The trustees in a Chapter X reorganization of Swan-Finch Oil Corporation applied to the District Court for the Southern District of New York for an order directing Doeskin Products, Inc. and Keta Gas & Development Company to turn over to them a certificate for all the outstanding stock of Keta, namely 1,140,390 common shares, and all of its assets, which they claim is the property of Swan-Finch.

The basic facts are virtually undisputed. Lowell M. Birrell who dominated Swan-Finch and the three other companies involved, caused the name of the registered owner, "Swan-Finch Oil Corporation," to be altered by striking "Oil" and typewriting over it the words "Gas Development." A similar alteration in handwriting was made on the certificate stub. Thereafter by treating the subsidiary Swan-Finch Gas Development Corporation as owner of the stock, by causing an unauthorized agreement for the exchange of stock to be executed between Gas Development and Doeskin and by causing the issuance of 700,000 shares of Doeskin stock to Gas Development which Birrell then had Gas Development's president hand over to him, Birrell has availed himself of the proceeds and Doeskin has become the registered owner of the stock.

The trustee's claim derives from the contention that the debtor never authorized the transfer of the Keta shares to the Doeskin company or to its own wholly-owned subsidiary, Gas Development, but that such transfer as was purportedly made was carried out by a fraudulent agent of both companies, Lowell M. Birrell. The trustees contend that Judge Palmieri erred in holding that they may recover the shares transferred by Birrell only if they restore to Doeskin the shares it issued to Birrell. We hold that the transaction by which the Keta shares were transferred to Doeskin was entirely without authorization; that the receipt by Gas Development's president did not constitute receipt by the debtor of the Doeskin stock, and that therefore the debtor may recover the Keta shares from Doeskin without returning the shares given up by Doeskin in receiving them.

Birrell's domination of the four companies which he accomplished through Mary B. Prior, his sister, Roy H. Callahan and others, is conceded. Apparently Birrell made and unmade directors and officers pretty much as he saw fit. The salient facts regarding the four dominated companies during the times in question may be briefly stated:

Swan-Finch Oil Corporation (Swan-Finch), a New York corporation with offices at 41 East 42nd Street, New York, was both a holding and an operating company, with 6,000 stockholders and assets of about $12,000,000. Its stock was traded on the open market. Until October 1, 1956 Birrell was a director and the principal executive officer and after that date he was also treasurer. Callahan was a director, a vice-president, and for a time in 1957 he was president. Mary Prior was a director, vice-president and secretary.

Swan-Finch Gas Development Corporation (Gas Development), a Pennsylvania corporation wholly-owned by Swan-Finch, had New York offices at 545 Fifth Avenue

where Birrell's law office was located, three short blocks away from 41 East 42nd Street. Birrell was a director, Callahan was a director and president and Mary Prior was a director, vice-president and secretary.

Keta Gas & Oil Company, a Pennsylvania corporation, was engaged in developing and drilling gas wells principally in western Pennsylvania. While it maintained offices at Bradford, Pennsylvania, its executive offices, at least after September 27, 1955, were at 41 East 42nd Street. Keta's assets were carried at about $4,000,000 at the time it was acquired by Swan-Finch in September 1955 and at $6,800,000 at the end of 1956. After Keta's acquisition Birrell became a director and the principal executive officer, Mary Prior became a director and secretary, and Callahan became a director and sometime later became president.

Doeskin Products, Inc., a New York corporation engaged in the manufacture and sale of paper products, also had its offices at 41 East 42nd Street. Doeskin had numerous stockholders and its stock was traded on the open market. Birrell was a director and the principal executive officer of Doeskin. Callahan was a director and president for a time, and Mary Prior was a director and secretary.

On September 27, 1955 Swan-Finch acquired all the outstanding 1,140,390 shares of Keta common stock and there was issued to it certificate #2 for those shares.

During the last few days of December 1956 Birrell's manipulations bore fruit and he secured possession of 700,000 shares of Doeskin's stock in return for the Keta stock. Although Birrell, his sister, Mary Prior, and Callahan were the three principal actors in the transactions, only Callahan was available as a witness. Sometime about September 1957 Birrell went to Cuba where he was later joined by his sister, Mary Prior, and these two concededly have been evading the jurisdiction of our courts.

But the main events and the inferences to be drawn therefrom seem beyond dispute.

On December 28, 1956 Birrell presented to a meeting of the Doeskin directors what purported to be a contract between Gas Development and Doeskin for the exchange of all the Keta stock in return for 700,000 shares of Doeskin stock. The contract was signed by Callahan for Gas Development and by Birrell for Doeskin on or about December 25, although it was dated October 5, 1956 and provided for a closing on November 15. Callahan testified he first heard of the proposal late in December and that he had not known that Keta had been transferred from Swan-Finch to Gas Development.

The Doeskin directors not dominated by Birrell had never heard of the contract and they objected. Three of them, Emanuel Katz, Harry Troilin and Alexander Blumenthal, immediately resigned. A fourth, Robert Six, left the meeting, and a fifth, William Erb, testified that he did not approve. As a quorum was no longer present the meeting was adjourned to December 31. The respondents produced alleged minutes which purport to show that the meeting was postponed to December 31, and December 31 minutes which purport to show that three directors were then present, Birrell, Callahan and Joseph Crosby, also Comptroller, and they recite approval of the contract at that meeting. Doeskin's president, Ralph Damp and directors Edward G. Brown and William Erb were never notified. Judge Palmieri's finding that no December 31 meeting ever took place is clearly right.

Birrell also caused the fabrication of minutes of a Swan-Finch directors' meeting of January 4, 1956, and of a Gas Development directors' meeting of January 26, 1956, which minutes record the approval of the transfer of the Keta stock from Swan-Finch to its subsidiary Gas Development. But it is abundantly established that no one, aside from Birrell and Mary Prior, had any inkling

that Keta was no longer a subsidiary of Swan-Finch. It is clear from the record that the alleged Swan-Finch meeting of January 4, 1956 and the alleged Gas Development meeting of January 26, 1956 never took place.

On December 31, 1956 Birrell and Callahan went to the 29 Broadway office of the Manufacturers Trust Company, Doeskin's transfer agent, to secure the issuance of the 700,000 Doeskin shares pursuant to the spurious contract. Birrell in the additional capacity as counsel to Doeskin gave his written opinion of the corporate regularity of the transaction and stated that the transaction was "for investment and no public offering is involved." Thereupon the bank issued seven certificates each for 100,000 shares of Doeskin common stock which were given to Callahan, president of Gas Development, who, at Birrell's request immediately handed them over to Birrell before they left the bank.

Apparently the altered certificate #2 for the Keta shares was turned over the same day, December 31, to Doeskin and, although it was never endorsed by anyone on behalf of Gas Development, Keta issued certificate #3 to Doeskin for 1,140,390 shares, dated December 31, 1956, and signed by Mary B. Prior as secretary and Callahan as president.

Sometime in January 1957 Callahan, as president of Gas Development, executed stock powers in blank at Birrell's request. From January 8 to March 28, 1957 the seven certificates for the Doeskin shares found their way to brokers in Canada. Thus except for Callahan's momentary token possession, as to which he was in no way authorized by the directors of Gas Development, there is no evidence that Gas Development ever received the Doeskin shares. Likewise there was no attempt to show that Callahan was authorized to execute the stock powers.

The first question presented by these facts is whether the debtor authorized the transaction by which the Keta

shares were transferred to Doeskin, and at the forefront of this question is the problem of which company, the debtor or its wholly-owned subsidiary, Gas Development, ought to be regarded as the shareholder. In the view we take of the case this preliminary question is not decisive, since in any event no greater authority existed for the transfer from the debtor to Gas Development than for the transfer to Doeskin, and in our view of the case the governing defect flows from the second transfer. We will therefore regard the debtor as the Keta shareholder, and direct our attention to the question whether it authorized the transfer to Doeskin.

Judge Palmieri expressly found on disputed evidence that there was no directors' meeting of the debtor with regard to the transfer of Keta shares, and that three of its six directors had no knowledge whatever of the dealings of Birrell and his cohorts with the stock. He appears nevertheless to have concluded that Birrell's conceded domination of the affairs of all the corporations concerned was a satisfactory substitute for such authorization. We think the law of New York, the state of incorporation of both transferor and transferee, is to the contrary.

Under the law of New York mere "domination" of a board of directors is not the equivalent of the assent of the board in cases where such assent is a legal condition of the transaction. See *Manson* v. *Curtis*, 223 N. Y. 313, 322-23 (1918); *McQuade* v. *Stoneham*, 263 N. Y. 323, (1934); *Long Park, Inc.* v. *Trenton-New Brunswick Theatres Co.*, 297 N. Y. 174 (1948).

Nevertheless the question remains whether the transaction was within the implied authority of Birrell, acting as president, without the assent of the directors. The law of New York on this question appears substantially unchanged since this court's decision in *Schwartz* v. *United Merchants & Manufacturers, Inc.*, 72 F. 2d 256 (2 Cir. 1934), where we held that such authority exists only as to

matters which are "usual" or "ordinary," and that the burden rests upon the party challenging the president's authority to show that the transaction was "unusual" or "extraordinary." What is usual or ordinary necessarily depends on the circumstances of the particular case, and in the circumstances here presented there can be no doubt that the transaction was extraordinary. Before the transaction took place Doeskin, an operating company, had 470,000 shares outstanding, of which the debtor held about 200,000, or about 40%. Had the transfer been properly carried through the debtor would then have held 900,000 of a total of 1,170,000 shares of Doeskin, or about 77%. For such an increase in its ownership of Doeskin, the debtor surrendered the Keta shares, of an estimated worth of approximately $6,800,000, or about one-half of the assets of the debtor. As to such a transaction it is clear that no authority existed by implication or appearance in a single corporate officer. Accordingly the transfer of the Keta shares was an entirely unauthorized transaction, and the issuance of Keta certificate #3 to Doeskin did not make it any more the shareholder of Keta than if it had been issued by a stranger.

We assume for purposes of this decision that as a result of the unauthorized nature of the transfer purportedly made by the debtor, it can recover the Keta shares from Doeskin, but that it can recover them only if it tenders back to Doeskin such benefit as it has received from the carrying out of the transaction. The question whether such a tender back is required in the present circumstances is not without considerable difficulty, e.g. compare *U. S. Fidelity & Guaranty Co.* v. *Neuburger*, 263 N. Y. 16 (1933), with *Appleton* v. *Citizens Bank*, 190 N. Y. 417, 421, aff'd 216 U. S. 196 (1909); *Losie* v. *Ken-Vic*, 43 N. Y. S. 2d 914, aff'd 44 N. Y. S. 2d 473 (A. D. 3d Dept. 1943); *Eisen* v. *Post*, 1 App. Div. 2d 344, rev'd on other grounds, 3 N. Y. 2d 518 (1957), but it need not be decided here in view of our decision of the ultimately decisive question of

whether or not the debtor received the Doeskin shares surrendered by the transfer agent.

Two New York cases establish that Callahan's receipt of the Doeskin certificates from the transfer agent did not amount to their receipt by the debtor. In the first the Court of Appeals held that an action for money had and received would not lie against a corporation whose agent had procured the plaintiff's check made out to the corporation, deposited it to the corporate account, and then made a withdrawal for his own benefit. Although the corporate accounts had thus been employed by the corporate president to secure the plaintiff's funds it was held that no receipt on the part of the corporation resulted because of the absence of corporate authorization and corporate knowledge of the transaction. *Credit Alliance Corp.* v. *Sheridan Theatre Co.*, 241 N. Y. 216 (1925). In the second the operative facts were substantially the same. *Matteawan Mfg. Co. v. Chemical Bank & Trust Co.*, 244 App. Div. 404 (1 Dept. 1935). The facts in the instant case differ only in the respect that in order to effect the transfer of the Doeskin shares Birrell had to command the assistance of Callahan. Since it amply appears that throughout Callahan was duped by Birrell and acted in effect as his alter ego, we do not think this a sufficient ground of distinction. We conclude therefore that mere possession of the Doeskin shares by Birrell or his confederates did not, under New York law, constitute the debtor a possessor of the shares.

Accordingly we hold that the debtor may recover the Keta shares without tendering back to Doeskin the shares with which Birrell apperently absconded, and therefore the decision below is reversed.

HAND, *Circuit Judge* (dissenting):

The Keta shares had been validly issued, but they were never transferred to Doeskin Products Inc. Birrell, who

was throughout the *deus ex machina* of the whole fraud, was not even president of the debtor, which was the registered shareholder of the shares. A majority of the debtor's directors had never agreed to their sale. The change on the face of the Keta certificate did not affect the debtor's rights in any way whatever; any subsequent transaction under the name of "Gas Development Company" was of as little legal significance as though it had been in the debtor's own name. Therefore I agree with my brothers that Doeskin Products, Inc. never became assignee of the Keta shares; it was not even a bona fide holder of the certificates. Nevertheless a certificate was issued for the shares in favor of Doeskin Products Inc., and I agree that the debtor is entitled to a cancellation of that certificate and to a new certificate which will be evidence of its right.

However, the transaction was in the form of an exchange and certificates were issued for 700,000 new shares of Doeskin Products Inc. in favor of "Gas Development Company" and these certificates were delivered to Callahan, the president of "Gas Development Company." The issue of these new shares was also unauthorized and invalid, just as the transfer of the Keta shares to Doeskin Products Inc. The question therefore arises whether the debtor's claim can be enforced except as a rescission of the exchange by restoring Doeskin Products Inc. to its former position. It is the law of New York that after such an exchange restoration by either party presupposes a return by the claimant of the consideration received; and this is true, not only when the transfer was unauthorized by the corporation's officials, as here, but when it was *ultra vires*. *Vought v. Eastern Building & Loan Association*, 172 N. Y. 508, 517, 518; *Appleton v. Citizens Central National Bank*, 190 N. Y. 417; 216 U. S. 196; *Losie v. Ken-Vic*, 43 N. Y. Supp. (2) 916, aff'd, 44 N. Y. Supp. (2) 473. This has also been the Federal doctrine, as appears in the often cited decision of the Su-

preme Court, *Central Transportation Co.* v. *Pullman's Palace Car Co.*, 139 U. S. 24, 60. Mr. Justice Gray there said of an *ultra vires* contract, "(i)n such case, however, the action is not maintained upon the unlawful contract, nor according to its terms; but on an implied contract of the defendant to return, or failing to do that, to make compensation for, property or money which it has no right to retain. To maintain such an action is not to affirm but to disaffirm the unlawful contract." For this reason the debtor may disaffirm the exchange and reclaim the Keta shares only on condition that it restores Doeskin Products Inc. to the equivalent of its position before the transfer.

The Doeskin certificates were delivered to Callahan, the president of "Gas Development" and it was by means of them, endorsed by Callahan that Birrell procured the certificates that he sold to third persons and embezzled the purchase money. Again it appears that under the law of New York the buyers got a good title to the shares in spite of the invalidity of their issuance. *Fifth Avenue Bank* v. *Forty-Second Street and Grand Street Ferry Co.*, 137 N. Y. 231; *Jarvis* v. *Manhattan Beach Co.*, 148 N. Y. 652, cited with approval in *Benenson* v. *National Surety Co.*, 260 N.Y. 299 at pp. 303-04.

The debtor replies that all these steps were a part of Birrell's fraudulent scheme and that of course is true.

The only issue between my brothers and me, so far as I can see, is whether the Doeskin shares were delivered to the debtor or to Birrell, for if they were delivered to Callahan it makes no difference that Birrell "dominated" him. Concededly the certificates for the 700,000 shares were delivered to Callahan, and, although it was in the name of the "Gas Development" company, that was the same as though it had been in the debtor's name. Indeed, Callahan was himself vice-president of the debtor at the end of 1956 when the delivery took place. I cannot therefore agree that the delivery, which was intended to be in conformity with the contract, was to Birrell.

whatever were his purposes. For that reason it seems to me that the case at bar falls within the decisions I have cited which hold that the injured party may not reclaim property unlawfully procured from him unless he restores any consideration he may have received.

My brothers rely upon the decision of the New York Court of Appeals in *Credit Alliance Corp.* v. *Sheridan Theatre Co.*, 241 N. Y. 216, as showing that the debtor never became so possessed of the Doeskin shares as to make their restitution a condition upon its recovery of the Keta shares. In the decision they cite the defendant corporation had by resolution provided that it should not borrow money except when authorized by the signatures of its president, Spiegel, and its treasurer, Rafferty. Spiegel drew up five notes which he signed as president and to which he forged Rafferty's name; hence they were not in fact obligations of the defendant at all. These five notes Spiegel then transferred to the plaintiff together with a certificate for 100 shares of the defendant's stock. In exchange the plaintiff gave "to Spiegel or some one representing him a check * * * payable to the order of the defendant corporation. This check Spiegel had certified and then he deposited it in a bank to the credit of the defendant. Almost immediately thereafter he drew a check of the defendant payable to his own order for the amount deposited, again forging the name of Rafferty. This check he deposited in a bank to his own credit." The Court of Appeals dismissed the plaintiff's complaint for "money had and received" for the following reasons among others. "The money, having been immediately withdrawn by Spiegel and converted to his own use without the corporation's knowledge of the transaction or that the funds had ever been placed to its credit, it enjoyed no benefit and exercised no dominion over the same."

In the case at bar both the transfer of the Keta shares to Doeskin and the issue of Doeskin shares to the debtor,

sub nomine, "Gas Development," were invalid, not being executed by the only persons authorized by either corporation to make them. The only difference between the two is that Doeskin kept the Keta shares, and the debtor disposed of the Doeskin shares. If the debtor had not done so, the debtor would certainly have been obliged to restore the Doeskin shares as a condition upon the recovery of the Keta shares since the transaction was an exchange, and a party seeking to rescind an exchange must restore the consideration or its equivalent. It is true that the Doeskin shares were sold and the proceeds were apparently embezzled by Birrell; but that cannot disguise the fact that they were issued to the debtor with the active connivance of other of the debtor's officials, and had become as much a part of its assets as the Keta shares are part of Doeskin's assets. Hence it follows that the proceeds of those shares are as much the property of the debtor as the unsold Keta shares are property of Doeskin. *Credit Alliance Corp.* v. *Sheridan Theatre Co.*, *supra* (241 N. Y. 216) depends, I think, upon the fact that Spiegel's transactions were not to be imputed to the defendant because no official of the defendant was privy to them at any stage. We should, I think, impose upon the debtor as a condition of any recovery the nearest possible equivalent of a cancellation of the newly issued Doeskin shares. As my view is not to prevail I shall not attempt to consider what should be deemed such an equivalent and indeed the parties have not discussed this aspect of the case. Therefore, although I would affirm the order so far as it directed a retransfer to the debtor of the Keta shares, I would make it conditional upon what the district court finds to be the nearest equivalent to cancellation of the Doeskin shares.

ORDER

UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

At a Stated Term of the United States Court of Appeals, in and for the Second Circuit, held at the United States Courthouse in the City of New York, on the twenty-fourth day of August one thousand nine hundred and fifty-nine.

Present:

Hon. LEARNED HAND, Circuit Judge,
Hon. J. WARREN MADDEN, Court of Claims Judge,
Hon. J. EDWARD LUMBARD, Circuit Judge.

In the Matter of

SWAN FINCH OIL CORP.,

Debtor

— THOMAS J. CRAWFORD & WILLIAM PETTIT, TRUSTEES,

Appellants,

DOESKIN PRODUCTS INC. & KETA GAS & OIL CO.,

Appellees.

Appeal from the United States District Court for the Southern District of New York.

This cause came on to be heard on the transcript of record from the United States District Court for the Southern District of New York, and was argued by counsel.

ON CONSIDERATION WHEREOF, it is now hereby ordered, adjudged, and decreed that the order of said District Court be and it hereby is reversed and the action remanded in accordance with the opinion of this court; with costs to the appellants.

A. DANIEL FUSARO
Clerk

APPENDIX C

WILLIAM D. PETTIT and THOMAS J. CRAWFORD,
Trustees-Appellants,

v.

DOESKIN PRODUCTS, INC. and KETA GAS & OIL COMPANY,
Appellees.

No. 244, Docket 25437.

United States Court of Appeals
Second Circuit.

On Petition Rehearing Filed Sept. 8, 1959.

Decided Oct. 13, 1959.

* * * *

Before HAND, Circuit Judge; MADDEN, Judge, United States Court of Claims,* and LUMBARD, Circuit Judge.

PER CURIAM.

The defendants—Doeskin Products, Inc. and Keta Gas and Oil Company—petition for a rehearing on the ground that we did not decide the validity of Judge Palmieri's ruling that he had summary jurisdiction over the controversy and that a plenary action was not necessary.

The defendants had made a cross-motion before the hearing, asserting that the court had no summary jurisdiction over the claim, and it is true that Judge Palmieri never entered any order denying this motion. However, his first conclusion of law made after the hearing was that he had "jurisdiction of the parties and of the subject matter of the proceeding" and the order on appeal which dismissed the trustees' petition was drafted in accordance with his direction that "an appropriate order will be en-

* Sitting by designation pursuant to the provisions of 28 U.S.C. § 291(a).

tered." There can be no question that this order, incorporating as it did, the conclusion of law just mentioned, was intended to deny the defendant's cross-motion that the court should require the trustees to bring a plenary action.

When the case came here on appeal we considered the merits of the trustees' claims and held that the debtor should "recover the Keta shares without tendering back to Doeskin the shares with which Birrell apparently absconded." We could not have so proceeded except on the assumption that the denial of the cross-motion to dismiss the summary proceeding was correct. The defendants did not appeal at all, although in one point of their brief (apparently provisionally accepting the decision below), they "submit that should a reversal or substantial modification be indicated herein, a 'plenary action' should be required instead of the instant proceeding." In short, they assert that, although they took no appeal from the order that denied them any "plenary action," they are entitled to review it in this proceeding because it was an error for the District Court to proceed on the merits at all. They may not so play fast and loose; if they meant to raise the point that the District Court was wrong to deny their cross-motion, they should have appealed from the order which denied it. Peoria & P. U. Railway Co. v. United States, 263 U.S. 528, 535, 536, 44 S.Ct. 194, 68 L.Ed. 427.

Petition denied.

ORDER

UNITED STATES COURT OF APPEALS SECOND CIRCUIT

At a Stated Term of the United States Court of Appeals, in and for the Second Circuit, held at the United States Courthouse in the City of New York, on the thirteenth day of October one thousand nine hundred and fifty-nine.

Present:

Hon. LEARNED HAND, Circuit Judge,
Hon. J. WARREN MADDEN, Court of Claims Judge,
Hon. J. EDWARD LUMBARD, Circuit Judge.

In the Matter of

SWAN FINCH OIL CORP.,
Debtor

THOMAS J. CRAWFORD & WILLIAM PETTIT, TRUSTEES,
Appellants.

v.

DOESKIN PRODUCTS INC. & KETA GAS & OIL CO.,
Appellees.

A petition for a rehearing having been filed herein by counsel for the appellees,

Upon consideration thereof, it is

Ordered that said petition be and hereby is denied.

A. DANIEL FUSARO
Clerk